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March 13, 2017

[redacted]

Marlene H. Dortch
Secretary
Federal Communications Commission
445 Twelfth Street, S.W.
Washington, DC 20554

Re: Proposed Resolution to Business Data Services Proceeding, WC Docket Nos. 16-143, 05-25, 15-247, RM-10593

Dear Ms. Dortch:

AT&T submits this letter to address how the Commission should finally resolve its decade-old review of the pricing flexibility rules for special access, a/k/a business data services ("BDS"). The current pricing flexibility rules, adopted in 1999, now apply only to DS1 and DS3 services offered over legacy TDM networks. Those services have grown increasingly competitive, particularly in recent years as the industry completes its transition to higher-speed, more flexible Ethernet services. Indeed, over the last decade cable companies have aggressively targeted the business services market with fiber-based Ethernet, Ethernet-over-HFC, and high-speed "best efforts" broadband.[1] Even Level 3, a historical proponent of regulation, recently conceded that the

[1] The industry's transition to Ethernet is irreversible and the legacy TDM services at issue are now in terminal decline. AT&T lost *more than* **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** *percent* of its DS1 business from non-affiliates just between January 2013 and October 2015. Declaration of Paul Reid ¶ 18 ("Reid 1/8/16 Decl."), attached to Brief of AT&T Inc. in Support of Its Direct Case, *Investigation of Certain Price Cap Local Exchange Carrier Business Data Services Tariff Pricing Plans*, WC Docket No. 15-247 (Jan. 8, 2016).

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BDS industry is "vibrant and competitive and will remain so."[2] Accordingly, the Commission should eliminate or relax price cap regulation of these legacy services where the data show that facilities-based competition has taken hold, which will remove needless regulatory barriers to investment and competition and facilitate the completion of the ongoing transition to next generation broadband services.

Both the *economics* and the *regulatory principles* that should guide those rule changes are clear. As to economics, the Commission, courts and economic experts have repeatedly confirmed that there is no justification for price cap regulation where competitors have deployed sunk investment, because the presence of such investment ensures that ILEC prices will remain at just and reasonable levels.[3] In this regard, the Commission, courts, the Department of Justice, and economic testimony have emphasized that it is not necessary that a competitor have a connection from its transport network to *every* single building in an area for that competitor to constrain ILEC prices in all buildings in that area.[4] Instead, competitors build transport networks to an area,

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[2] *See* Consolidated Application to Transfer Control of Domestic and International Section 214 Authorizations, *Level 3 Communications, Inc., Transferor and CenturyLink, Inc., Transferee*, WC Docket No. 16-403, at B-3 (Dec. 12, 2016).

[3] *See, e.g., WorldCom, Inc.* v. *FCC*, 238 F.3d 449, 458-59 (D.C. Cir. 2001) ("the presence of facilities-based competition with significant sunk investment makes exclusionary pricing behavior costly and highly unlikely to succeed," because "that equipment remains available and capable of providing service in competition with the incumbent, even if the incumbent succeeds in driving that competitor from the market" (internal quotations omitted)); Fifth Report & Order & Further Notice of Proposed Rulemaking, *Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers*, 14 FCC Rcd. 14221, ¶ 80 (1999) ("*Pricing Flexibility Order*") (once a *facilities-based* competitor has "entered the market and cannot be driven out, rules to prevent exclusionary pricing behavior are no longer necessary"), *aff'd WorldCom, Inc.* v. *FCC*, 238 F.3d 449, 458-59 (D.C. Cir. 2001). ); *see also* Mark Israel, Daniel Rubinfeld, and Glenn Woroch, Competitive Analysis of the FCC's Special Access Data Collection, *Special Access Rates for Price Cap Local Exchange Carriers et al.*, WC Docket No. 05-25, RM-10593, at 14 (Jan. 26, 2016) ("IRW First White Paper") ("The Commission's approach appropriately recognizes that once rivals have incurred sunk costs in network facilities . . . there is little basis for concern about exclusionary or predatory tactics."); Mark Israel, Daniel Rubinfeld, and Glenn Woroch, Analysis of the Regressions and Other Data Relied Upon in the Business Data Services FNPRM And a Proposed Competitive Market Test: Second White Paper, *Business Data Services in an Internet Protocol Environment et al.*, WC Docket Nos. 16-143, 05-25, RM-10593, at 39-40 (Jun. 28, 2016) ("IRW Second White Paper") ("As a matter of economics, price cap regulation is unnecessary and is, in fact, counterproductive in areas where rivals have deployed competing facilities-based networks."); Mark Israel, Daniel Rubinfeld, and Glenn Woroch, Analysis of the Regressions and Other Data Relied Upon in the Business Data Services FNPRM And a Proposed Competitive Market Test: Third White Paper, *Business Data Services in an Internet Protocol Envorinment et al.,* WC Docket Nos. 16-143. 15-247, 05-25, RM-10593, at 2 (Aug. 9, 2016) ("IRW Third White Paper").

[4] *See, e.g.*, Memorandum Opinion and Order, *Applications of XO Holdings and Verizon Communications Inc. For Consent to Transfer Control of Licenses and Authorizations*, WC Docket No. 16-70, DA 16-1281, ¶ 22 (Nov. 16, 2016) ("*Verizon/XO Merger Order*") (finding no competitive harm in buildings where there is a nearby

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compete for customers in buildings in that area, and then construct connections to the buildings where they win customers. BDS customers are "sophisticated purchasers of telecommunications services" that can "find[] competitive alternatives where they exist,"[5] which ensures that no competitor can charge rates that fall outside the Communications Act's broad zone of "reasonableness."[6] The question in the current proceeding, then, is not *whether* price cap regulation should be eliminated in areas where competitors have deployed sunk facilities; rather, the task is simply to use the Commission's unprecedented data collection and the rulemaking record to determine *where* such facilities exist today and extend pricing flexibility relief accordingly.

With respect to regulatory principles, the Commission should adopt the simplest and most easily administrable rules that avoid imposing unnecessary costs or complexity. Unnecessary regulatory requirements on these declining DSn services could produce many different kinds of costs. Most obviously, unnecessary price and term regulation artificially prolongs reliance on these legacy services, dampening demand for Ethernet services and retarding badly needed investment in next-generation broadband facilities. Such rules also create needless frictions in the marketplace. The collective drag on the industry from these unnecessary and sometimes counterproductive costs are substantial: they block meaningful increases in consumer welfare, innovation, and jobs.

In addition, in choosing between different approaches to achieving its regulatory objectives, the Commission should favor approaches that can be readily implemented without undue costs or delay. CLECs have frequently argued in this proceeding that the Commission should change its entire pricing flexibility regime to a system that provides relief on a geographic unit smaller than an MSA, such as a county or census block. As AT&T has explained (and as detailed further below), if the Commission made any such shift mandatory on all price cap LECs, AT&T would have to spend millions of dollars and many months overhauling its billing (and related) systems. Such costly and disruptive changes would not serve any business purpose, but would be necessary solely to comply with a regulatory edict – and all for DSn services that will

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competitor); *WorldCom, Inc.*, 238 F.3d at 458-59 (endorsing the Commission's pricing flexibility rules adopting a test based on nearby "sunk facilities"); Memorandum Opinion and Order, *AT&T Inc. and BellSouth Corp. Application for Transfer of Control*, 22 FCC Rcd. 5662, ¶¶ 41-42, 46 & nn.111-14 (2007) (describing and adopting "screens" employed by DOJ to determine whether a building could be served by alternative facilities, which recognize that competitors with facilities near a building can and do compete for customers in that building).

[5] *Pricing Flexibility Order* ¶ 155.

[6] *See also id.* ¶ 153 n.389 (explaining that "it is unnecessary to extend the efficiency incentives of price cap regulation to services offered on a 'contract-type basis'") (citing Second Report and Order, *Policy and Rules Concerning Rates for Dominant Carriers*, 5 FCC Rcd. 6786, ¶ 193 (1990) ("*LEC Price Cap Order*")).

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likely be retired altogether early in the next decade. Even if it were the case that there was some marginal benefit to a more granular competitive market test, any such benefit would be eclipsed by the increased costs and delays that would result from the implementation of such a test. But, as discussed below, there is no such marginal benefit because the MSA test AT&T proposes improves upon the existing MSA test by limiting relief to MSAs with near-ubiquitous competition.

In short, the Commission should focus on the hard facts of competition and where and what kind of regulation is still desirable. The 2013 data collection, along with other data in the record, show that competitors have deployed their own facilities-based networks within reach of the vast majority of locations where BDS demand exists across the nation. While not perfect and clearly not inclusive of the explosive growth in cable-provisioned BDS, the 2013 data collection provides more than enough concrete support for the Commission to act here and close this decade-old proceeding. Indeed, those data confirm that the triggers were overly conservative – and that there are many additional areas where expanded pricing flexibility would be warranted.

As explained below, the Commission should take the following steps based on the 2013 dataset collected by the Commission:

- **DS1/DS3 Transport**:
    - The Commission should grant Phase II pricing flexibility to all DS1/DS3 transport services. The record overwhelmingly shows that competitors have deployed their own interoffice transport networks in large and small cities, and there are often a dozen or even two dozen such competitors. No party to this proceeding has made any serious attempt to show that price cap regulation of transport remains necessary.
- **DS1/DS3 Channel Terminations**:
    - Although the record clearly supports nationwide Phase II relief for channel terminations as well, at a minimum:
        - The Commission should immediately grant Phase II relief in all MSAs in which the 2013 data show that at least 80% of locations served by ILECs in the MSA are within 2,000 feet of at least one competitor.
        - The Commission should retain the MSA as the geographic basis for relief. MSAs still strike the most appropriate balance between accuracy and administrative costs, especially if the Commission adopts AT&T's proposed standard, which limits relief to MSAs characterized by near

ubiquitous competition (*i.e.,* granting Phase II relief only in MSAs where at least 80% of the buildings are within 2000 feet of existing competitive facilities). The Commission's goal should be to reduce unnecessary administrative burdens, and imposing more geographically granular areas of relief as some have proposed would require the ILECs to invest in expensive and time-consuming retrofitting of its billing and other systems that would make no sense for these rapidly declining services.

- The Commission should immediately grant Phase I pricing flexibility to all remaining DS1 or DS3 channel termination services, including those with no pricing flexibility relief. Phase I pricing flexibility permits *downward* pricing flexibility, *e.g.*, the ability to enter into contract tariffs that contain customer-specific term, volume, and other discounts, and there is no reason to deny that flexibility anywhere in the country.

- **Price Cap/X-Factor**:

  - The X-Factor that has been in effect since 2005, which was set equal to inflation, has resulted in productivity adjustments that are almost exactly equal to the observed communications sector productivity over that period as measured by the BLS KLEMS methodology, which is the only defensible method proposed in the *Notice*.

  - Because of this, the Commission should either maintain the current X-Factor (set equal to inflation), or adopt BLS KLEMS as the correct methodology for calculating the X-factor going forward, which would support a new X-Factor of no more that 2.0 percent.

- **Ethernet**:

  - The Commission should affirm that the marketplace for Ethernet (and all other high-capacity services for which ILECs have obtained forbearance) is highly competitive and that *ex ante* rate regulation for such services is unnecessary.

## I. THE COMMISSION SHOULD EXTEND PHASE II FLEXIBILITY TO DSn TRANSPORT SERVICES ON A NATIONWIDE BASIS.

The Commission should grant Phase II relief for all DSn transport services nationwide. The Commission's 2013 data collection shows that competitive transport networks are now

essentially ubiquitous, and no party to this proceeding has made any serious attempt to show otherwise.

The record clearly shows that transport is competitive. For all MSAs, as of 2013, competitive providers have deployed competing transport networks in more than 95% of census blocks with special access demand.[7] Facilities-based transport competition is extremely mature and extensive. The 2013 fiber maps that the CLECs submitted in response to the Commission's mandatory data requests show that in many large MSAs more than twenty competitive providers have deployed competing fiber transport facilities.[8] For example:

| MSA | Competitive Providers with Fiber Facilities within the MSA[9] |
|---|---|
| Atlanta-Sandy Springs-Roswell, GA | 25 |
| Chicago-Naperville-ELGIN, IL-IN-WI | 28 |
| Dallas-Fort Worth-Arlington, TX | 25 |
| Detroit-Warren-Dearborn, MI | 16 |
| Houston-The Woodlands-Sugar Land, TX | 22 |
| Los Angeles-Long Beach-Anaheim, CA | 15 |
| Memphis, TN-MS-AR | 21 |
| Miami-Fort Lauderdale-West Palm Beach, FL | 14 |
| St. Louis, MO-IL | 22 |
| Washington-Arlington-Alexandria, DC-VA-MD-WV | 24 |

[7] Mark Israel, Daniel Rubinfeld & Glenn Woroch, Competitive Analysis of the FCC's Special Access Data Collection, *Special Access Rates for Price Cap Local Exchange Carriers; AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, WC Docket No. 05-25, RM-10593, at 22-23 (filed Jan. 27, 2016) ("IRW 1/27/16 White Paper").

[8] Letter from James P. Young (representing AT&T) to Marlene H. Dortch (FCC), dated October 25, 2016, at 5 ("AT&T 10/25/16 *Ex Parte*") (including table).

[9] This table identifies the total number of competitive providers that reported having deployed "Fiber Facilities" in response to Question No. II.A.5 (CLEC fiber maps) of the Commission's data requests. The metrics in this chart exclude providers that reported having a "node" in an MSA but no fiber facilities. It also excludes cable HFC facilities.

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Indeed, the data show that even smaller MSAs very often have a large number of competitors with fiber networks. Second-tier MSAs very often boast over a dozen separate competitive providers with fiber networks.[10] And the record shows the same level of competition occurs in areas that have not received Phase II transport relief.[11]

Tellingly, no party to this proceeding has made any serious attempt to show that DSn transport should remain under price cap regulation. To the contrary, historical proponents of regulation have admitted that they have access to competitive transport facilities. XO, for example, conceded early that it "sees considerable competition for transport . . . There are many competitors for transport service in [central business districts] because numerous CLECs frequently are collocated in the offices where XO is located."[12] XO acknowledged that "it is feasible for XO to combine channel terminations from the ILEC with transport from a competitive provider."[13] Similarly, Windstream's company declarants have testified that Windstream typically self-supplies "Ethernet network access [*i.e.*, transport]," explaining that "Ethernet network access includes transport over Windstream's core network as well as long-haul, intercity transport."[14] They have also explained that "[o]nce the customer's traffic goes across the NNI, it is on

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[10] Examples include Birmingham, Alabama (14), Augusta, Georgia (17), Little Rock, Arkansas (12), Waco, Texas (12); San Diego, California (13), and South Bend, Indiana (14). Letter from Keith M. Krom (AT&T) to Marlene H. Dortch (FCC), *Business Data Services in an Internet Protocol Environment, et al*., WC Docket Nos. 16-143, 15-247, 05-25, RM-10593, at 3-4 (Nov. 10, 2016).

[11] Examples include Anniston, Alabama (10), Vallejo/Fairfield, Napa, California (10), and Beaumont/Port Arthur, Texas (10), among many others.

[12] Declaration of Michael Chambless ¶ 10 ("Chambless 1/27/16 Decl."), attached to comments of XO Communications, LLC On The Further Notice of Proposed Rulemaking, *Special Access for Price Cap Local Exchange Carriers; AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, WC Docket No. 05-25, RM-10593 (Jan. 27, 2016) ("XO 1/27/16 Comments").

[13] Chambless 1/27/16 Decl. ¶ 11; *see also id*. at 22 ("XO and the industry in general use transport and channel terminations for distinct reasons," and the "Commission has recognized this product distinction in numerous decisions and placed Dedicated Service channel terminations and transport in different product markets.").

[14] Declaration of David Schirack and Mike Baer, ¶ 13 ("Schirack/Baer 6/28/16 Decl."), attached as Attachment A to Comments of Windstream Services, LLC On The Further Notice of Proposed Rulemaking, *Business Data Services in an Internet Protocol Environment, et al.*, WC Docket Nos. 16-143, 15-247, 05-25, RM-10593 (Jun. 28, 2016) ("Windstream 6/28/16 Comments"); *see also* Reply Comments of Windstream Services, LLC, *Special Access for Price Cap Local Exchange Carriers, et al.*, WC Docket No. 05-25, RM-10593, GN Docket No. 13-5, at 13 (Feb. 19, 2016) ("Windstream 2/19/16 Reply") (admitting that "much of this fiber was intended to serve as transport rather than to provide last-mile connectivity").

Windstream's network, over which Windstream provides the middle-mile transport to one or more Windstream offices or another carrier's office where Windstream has collocated equipment."[15]

Indeed, the CLECs' arguments and evidentiary showings take for granted that CLECs have their own fiber transport networks and instead have focused almost entirely on the feasibility of deploying channel terminations.[16] For example, Level 3's arguments concerning competition have been expressed solely in terms of how many competitors can build a "loop" or a "connection" to a building from their fiber transport networks,[17] and its fact witness presented an analysis expressly limited to "estimat[ing] the maximum distance in linear feet that Level 3 finds it economically justified to construct fiber connections between a splice point *on Level 3's transport network* and the location of a Business Data Service customer."[18] Sprint's arguments similarly have focused on the distances CLECs are willing to extend laterals from the "splice points" of "transiting fiber."[19]

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[15] Declaration of David Schiack, Mike Baer and Samuel Bushey, ¶ 11 ("Schiack/Baer/Bushey 8/9/16 Decl."), attached as Attachment C to Reply Comments of Windstream Services, LLC On The Further Notice of Proposed Rulemaking, *Business Data Services in an Internet Protocol Environment, et al.*, WC Docket Nos. 16-143, 15-247, 05-25, RM-10593 (Aug. 9, 2016) ("Windstream 8/9/16 Reply"); *see also* Declaration of Robert D. Willig, ¶ 30 (Willig 8/9/16 Decl.") ("[t]he wholesale purchaser that uses the ILEC's Ethernet connection to reach a customer premise for the provision of retail services to the customer would use its own middle-mile, rather than the ILEC's middle mile"), attached as Attachment B to Windstream 8/9/16 Reply.

[16] Comments of Birch, EarthLink, and Level 3, *Business Data Services in an Internet Protocol Environment, et al.*, WC Docket Nos. 16-143, 15-247, 05-25, RM-10593, at 19 (Jun. 28, 2016) ("Level 3 6/28/16 Comments") (arguing that "competition in the provision of Business Data Services exists only where reasonably efficient competitive carriers can be expected to deploy loop facilities to a customer location").

[17] *Id.* at 18-19 & n.6; *see also id.* at 28 (framing the competitive analysis as whether Level 3 can "deploy loops").

[18] Declaration of John Merriman on Behalf of Level 3 Communications, LLC, ¶ 2 ("Merriman 6/27/16 Decl.") (emphasis added), attached as Appendix to Level 3 6/28/16 Comments; *see also id*. ¶ 5 (fact witness at pains to "emphasize that the construction feasibility limits shown in the table are to be measured from a splice point on Level 3's *transport network*, not merely from any point on the relevant fiber route" (emphasis added); *see also* Level 3 6/28/16 Comments at 20 (arguing that the question whether loop can be constructed should be judged in part based on whether the location is "near a point in their fiber transport facilities from which a connection can be deployed").

[19] Comments of Sprint Corp., *Business Data Services in an Internet Protocol Environment, et al.*, WC Docket Nos. 16-143, 15-247, 05-25, RM-10593, at 6-11 (June 28, 2016) ("Sprint 6/28/16 Comments"); *see also* Reply Comments of Sprint Corp., *Business Data Services in an Internet Protocol Environment, et al.*, WC Docket Nos. 16-143, 15-247, 05-25, RM-10593, at 6 (Aug. 9, 2016) ("Sprint 8/9/16 Reply Comments") (argument that "'fiber presence equals competition' . . . must be rejected [because] . . .significant barriers to entry prevent competitive carriers from deploying connection to most locations" (internal quotations omitted)). Sprint's economic experts have likewise focused on how many competitors have constructed connections to individual locations. Declaration of William P. Zarakas and Susan M. Gately, ¶¶ 17-18 ("Zarakas/Gately 1/21/16 Decl."), attached to Comments of Sprint Corp.,

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Notably, the Commission's *Suspension Order* in 2012, which led to the current proceeding, was also based almost entirely on a concern about a possible lack of competition for channel terminations, not transport.[20] The 2016 *Notice*, too, barely discusses transport. In the rare instances it does, it acknowledges significant differences between transport and channel terminations for TDM services. The Commission notes that "non-cable operators typically do not ubiquitously deploy connections to locations in a local geographic area," but "[t]hey instead invest in transport within a local area based on potential demand and then rely on a mix of facility-based deployments and leased lines to connect end-user locations to their network facilities."[21] This description of CLEC networks, and the Commission's subsequent discussion of "barriers to entry," squarely focus the inquiry on the extension of laterals to individual buildings.[22] Indeed, the Commission's expert, Professor Rysman, did not even perform separate regression analyses to test competition for transport. As the Commission explained, "[c]onnections that are strictly for transport between wire centers were [] removed" from Professor Rysman's analysis, "because the cost structure behind providing transport is likely to be substantially different from providing service to end-user premises and therefore would make comparisons of prices less meaningful."[23]

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*Special Access for Price Cap Local Exchange Carriers; AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, WC Docket No. 05-25, RM-10593 (Jan. 27, 2016) ("Sprint 1/27/16 Comments"); Declaration of Stanley M. Besen and Bridger M. Mitchel, ¶¶ 25-26 ("Basen/Mitchel 1/27/16 Decl."), attached to Sprint 1/27/16 Comments; *see also* Further Supplemental Declaration of William P. Zarakas, ¶ 13 ("Zarakas 8/9/16 Decl."), attached to Sprint 8/9/16 Reply Comments.

[20] Report and Order, *Special Access for Price Cap Local Exchange Carriers*, 27 FCC Rcd. 10557, ¶ 68 (2012) ("*Suspension Order*") ("Evidence submitted to the Commission since 1999 calls into question the Commission's prediction that collocators would eventually build their own channel terminations to end users."); *id*. ¶ 79 (noting that "the staff analysis of specific data highlighting problems with the MSA was restricted to channel terminations to end users"); *see also* Tariff Investigation Order and Further Notice of Proposed Rulemaking, *Business Data Services in an Internet Protocol Environment et al.*, WC Docket Nos. 16-143, 15-247, 05-25, RM-10593,¶ 28 (rel. May 2, 2016) ("*Notice*"). The Commission nonetheless adopted a freeze on the transport triggers as well, based on maps in the record suggesting that LEC transport networks might not extend throughout the entire geography of MSAs. *Id.*

[21] *Notice* ¶ 54.

[22] *See, e.g., id.* ¶¶ 224-27.

[23] *Id.*, Attachment 1, pg. 244 ("These were identified as connections that do not list a location ID for any of the billing elements in the billing table."). Professor Rysman included mileage charges in his analysis, but only when the channel terminations and transport had the same bandwidth; he ignored circuits in which the channel terminations were multiplexed onto higher capacity transport. As Drs. Israel, Rubinfeld, and Woroch previously explained, this focus had the effect of overstating the average price of circuits. *See* IRW Second White Paper at 18.

Even after acknowledging these differences, neither Professor Rysman nor the Commission staff ever ran regressions isolating transport services.[24]

Granting nationwide Phase II relief for transport would serve the goal of keeping the pricing flexibility rules administrable, because the ILECs already treat transport services and channel termination services separately under the existing pricing flexibility rules. Reclassifying all transport services as Phase II would be a simple change in an ILEC's billing and ordering systems, similar to the changes they make after each pricing flexibility application grant.

## II. THE COMMISSION SHOULD IMMEDIATELY EXTEND PHASE II RELIEF FOR CHANNEL TERMINATIONS TO ADDITIONAL MSAS AND GRANT PHASE I RELIEF TO ALL REMAINING AREAS.

The Commission should also expand Phase II relief for channel terminations. The record evidence confirms that the existing, more stringent "triggers" for channel terminations were too conservative, retaining price cap regulation where it is not warranted, including in many of the largest and most competitive cities in the nation (*e.g.*, Chicago and New York).[25] Accordingly, the Commission should immediately grant Phase II relief in any MSA in which the 2013 data show that 80 percent of the locations served by ILECs are within 2000 feet of at least one competitor, and it should immediately grant Phase I relief in all other areas. Moreover, as explained below, the Commission should retain the MSA as the geographic basis of relief to avoid forcing ILECs to invest millions of dollars and months of company time to implement complex changes to their billing, ordering, and other systems for the sole purpose of complying with regulatory requirements relating to these rapidly declining services.

*Economic Basis for Channel Termination Relief*. Any sound economic assessment of channel terminations must begin by recognizing how competition occurs in this marketplace. BDS providers deploy facilities in areas where they identify demand for BDS and then compete for customers in nearby locations. In most cases, competing providers construct connections to a location only *after* they have won a customer there. For these reasons, virtually all of the economic

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[24] The *Notice*'s only other reference to transport is the claim that "[t]oday, competitors, and even incumbent LECs with their forborne services, do not typically offer consumers BDS by charging a customer separately for transport, last-mile access, and channel mileage" but "instead offer connectivity at certain bandwidth levels and performance guarantees and packaged communications solutions that include a transmission component to meet the demands of different types of customers." *Id.* ¶ 282. This reference to the ILECs' *forborne* services, however, makes clear that the Commission is referring here only to the ILECs' Ethernet and high-capacity TDM services. ILEC tariffs for DS1s and DS3s today contain separate charges for channel terminations and transport, just as they did at the time of the *Pricing Flexibility Order*.

[25] *See, e.g.,* IRW First White Paper, Table C-MSA.

testimony in this proceeding agrees that "a comprehensive assessment of the extent of BDS competition at any location must take into account facilities deployed at that specific location as well as any networks that are in close proximity to that location."[26] This approach has also been endorsed by the Commission, Courts, and the Department of Justice.[27]

There has been a consensus throughout this proceeding that competitive providers compete for customers in buildings that are within about a half of a mile (2,640 feet) of their networks. Indeed, one of the "key findings" in the *Notice* is that "fiber-based competitive supply within at least half a mile generally has a material effect on prices of BDS . . . ."[28] Professor Baker – the economist hired by the CLECs – has stated (citing record evidence) that competitors typically compete for customers in buildings within about a half mile of their network facilities.[29] Professor Rysman, the Commission's economist, made similar findings.[30]

These findings are firmly grounded in the CLEC data. For example, the 2013 data indicate that many of Level 3's building connections are actually at distances beyond **[BEGIN HIGHLY**

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[26] IRW Third White Paper at 1; *see also* Marc Rysman, Empirics of Business Data Services: White Paper, at 218-19 ("Rysman White Paper"), attached as Appendix B to the *Notice*; Declaration of Jonathan B. Baker on Market Power in the Provision of Dedicates (Special Access) Services, *Special Access Rates for Price Cap Local Exchange Carriers; AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Service*, WC Docket No. 05-25, RM-10593, ¶¶ 39-40, 43 (filed Jan. 27, 2016) ("Baker 1/27/16 Decl.").

[27] *See* Memorandum Opinion and Order, *Applications of XO Holdings and Verizon Communications Inc. For Consent to Transfer Control of Licenses and Authorizations*, WC Docket No. 16-70, DA 16-1281, ¶ 22 (Nov. 16, 2016) ("*Verizon/XO Merger Order*") (finding no competitive harm in buildings where there is a nearby competitor); *WorldCom, Inc.*, 238 F.3d at 458-59 (endorsing the Commissions pricing flexibility rules adopting a test based on nearby "sunk facilities"); Memorandum Opinion and Order, *AT&T Inc. and BellSouth Corp. Application for Transfer of Control*, 22 FCC Rcd. 5662, ¶¶ 41-42, 46 & nn.111-14 (2007) (describing and adopting "screens" employed by DOJ to determine whether a building could be served by alternative facilities, which recognize that competitors with facilities near a building can and do compete for customers in that building).

[28] *Notice* ¶¶ 161-62. Moreover, the *Notice* correctly acknowledges that, in many instances, competitors are willing to extend laterals even farther. For example, a provider may be willing to build out greater distances if connecting to a customer in the building may lead to winning additional business in other buildings (either nearby or not) or if it obtains a long-term commitment. *Id.* ¶ 212.

[29] Declaration of Jonathan B. Baker on Market Power in the Provision of Dedicated (Special Access) Services, *Special Access for Price Cap Local Exchange Carriers; AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Service*, WC Docket No. 05-25, RM-10593, ¶ 43 (Apr. 14, 2016) ("Baker 4/14/16 Decl.").

[30] Mark Rysman, Empirics of Business Data Services, White Paper, WC Docket No. 05-25, at 11 (as revised June 2016) ("Revised Rysman White Paper") (citing record evidence that CLECs build out "a quarter to a half mile"), *available at* https://apps.fcc.gov/edocs_public/attachmatch/DOC-340040A6.pdf.

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**CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**.[31] Of the ones that are closer, **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of the locations with bandwidth demand below 10 Mbps are more than 2,350 feet from the nearest node, **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of Level 3's connections to locations with bandwidth demand between 10 Mbps and 50 Mbps are more than 2,500 feet from the nearest node; **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of Level 3's connections to locations with demand between 50 and 100 Mbps are more than 1,900 feet from the nearest node; and **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of Level 3's connections to locations with demand between 100 Mbps and 200 Mbps are more than 2,300 feet from nearest node. As Drs. Israel, Rubinfeld, and Woroch have shown, the same pattern holds for all CLECs.[32]

CLEC testimony further reinforces these findings. For example, Windstream submitted testimony explaining that it extends fiber to buildings that are within **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** of its fiber facilities and that **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**[33] Similarly, XO's Vice President of Access Management and Implementation stated that, as "a rule of thumb" XO will compete for customers and build laterals to buildings that are within **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** linear feet of its fiber facilities.[34] And the same goes for ILECs: for example, AT&T showed that its internal engineering guidelines require AT&T to engineer its network to maintain lateral distances at or below about **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]**

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[31] IRW Third White Paper at 34 (noting that the fact that many Level 3 locations were not near a node suggests that Level 3 either under-reported node locations, or does not always use splice points/nodes when extending lateral connections to buildings, or builds out from nodes at distances longer than the 1,000 meters captured by the FCC's building-distance-to-node crosswalk table).

[32] *Id.* at 10-11.

[33] Declaration of Dan Deem, Douglas Derstine, Mike Kozlowski, Arthur Nichols, Joe Scattareggia, and Drew Smith, ¶ 51 ("Deem *et al.* 1/27/16 Declaration"), attached as Attachment A to the Comments of Windstream Services, LLC, *Special Access for Price Cap Local Exchange Carriers, et al.,* WC Docket No. 05-25, RM-10593, GN Docket No. 13-5 (Jan. 27, 2016) ("Windstream 1/27/16 Comments").

[34] Declaration of George Kuzmanovski ¶ 24 ("Kuzmanovski Decl."), attached to XO 1/27/16 Comments. *See also* Chambless 1/27/16 Decl. ¶ 26 (XO builds out to buildings within **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** feet of its facilities).

[35] *See* Letter from Christopher T. Shenk (representing AT&T) to Marlene H. Dortch (FCC), *Special Access for Price Cap Local Exchange Carriers; AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent*

At its most basic level, then, the task in identifying areas where price cap regulation of channel terminations should be eliminated is simply identifying those areas where ILEC buildings are within a half mile of one or more competitors. On that standard, the record amply supports *nationwide* Phase II relief for channel terminations, because almost every building where an ILEC has a BDS customer is within a half mile of at least one competitor.[36] Nonetheless, AT&T proposes a more conservative standard, under which the Commission would immediately grant Phase II pricing flexibility only in those MSAs in which, according to the 2013 data, at least 80 percent of the locations in which ILECs have BDS connections in that MSA are within 2,000 feet of at least one other competitor's network (rather than the half mile).

This more conservative standard guarantees that Phase II relief is provided only where the Commission would be especially confident that competition is essentially ubiquitous. AT&T's proposed standard is far more precise and granular than the Commission's original triggers. Those triggers permitted Phase II pricing flexibility in MSAs where a competitor had collocated facilities in 65 percent of the wire centers. The D.C. Circuit properly upheld the use facilities-based collocations, and the 65 percent standard, as reasonable indicators of channel termination competition[37] (and, indeed, those rules proved to be under-inclusive in providing the necessary relief). AT&T's proposed standard here, by contrast, would rely on granular, *building-level* data, and require confirmation that a far higher percentage (80 percent) of those specific *locations* are in fact well within range of at least one facilities-based competitor.

For these legacy, TDM-based services, pricing almost always occurs on an MSA-wide (or even larger-area) basis. Accordingly, the Commission can reasonably conclude that competitive pricing will prevail throughout any MSA in which the overwhelming majority (80 percent) of the locations are subject to nearby facilities-based competition. Moreover, the Commission's data

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*Local Exchange Carrier Rates for Interstate Special Access Services,* WC Docket No. 05-25, RM 10593, at 11-12 (March 21, 2016) ("AT&T 3/21/16 *Ex Parte*").

[36] Second Supplemental Declaration of Mark Israel, Daniel Rubinfeld and Glenn Woroch, *Special Access for Price Cap Local Exchange Carriers*; *AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, WC Docket No. 05-25, RM-10593, ¶¶ 5-6 (Apr. 20, 2016) ("IRW 4/20/16 Decl.") (data collection shows that, as of 2013, about half of the buildings served by ILECs were within 88 feet (0.017 miles) of at least one CLEC's fiber facilities, 75% were within 456 feet (0.086 miles), 90% were within about 1,107 feet (0.21 miles), and virtually all (98.7 percent) were within a half mile); *see also id.* ¶ 14 (same is true of *demand* (measured by bandwidth; about 98 percent of BDS bandwidth served by large ILECs is located in buildings that are less than a half mile from at least one other provider's network, and even 90 percent of AT&T's sub-50 Mbps bandwidth is within a half mile of competitive fiber).

[37] *WorldCom*, 238 F.3d at 458-59 (upholding the triggers); IRW First White Paper, Table C-MSA (demonstrating that original triggers failed to grant Phase II pricing flexibility in many MSAs, including Chicago and New York, where nearly all businesses were addressable by competitive facilities).

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show that, in MSAs in which 80 percent of the locations are subject to competition, those buildings typically account for far more than 80 percent of all demand – providing further confirmation that a test focusing on 80 percent of *locations* would be quite conservative in identifying MSAs in which virtually all *services* are subject to competition. Indeed, AT&T's test is all the more conservative insofar as it relies on the 2013 data collection, which does not capture the rapid growth and investment in Ethernet and cable services that has occurred in the intervening years. For all these reasons, the MSA test AT&T proposes should ensure competitive constraints for all TDM-based services accorded Phase II pricing flexibility. And in all events, any BDS customer would be free to challenge the rates, terms and conditions of service under Sections 201 and 202. Under these circumstances, the costs of force-fitting a more granular competitive market test would far exceed its benefits.

In the unlikely event that these factors leave tiny pockets of locations unprotected in these highly competitive MSAs, customers in those areas will still have the ability to assert claims under Sections 201 and 202.

*Inclusion of All Relevant Competitors, Including Cable "Best Efforts" Services*. In applying this competitive market standard, the Commission should make sure that it accounts for all relevant competitors. There has been broad agreement for some time that the test should include all fiber-based and copper-based Ethernet facilities offered by ILECs, CLECs and cable companies, and HFC-based Ethernet services offered by cable companies. But contrary to some parties' arguments, the Commission should also include "best efforts" services offered by cable companies over HFC facilities.

There is no sound basis for excluding cable "best efforts" services as of 2017. Such "best efforts" services typically offer speeds of 100 Mbps or more, which *far* surpass the speeds available from legacy DS1 and DS3 services, and often at prices below those of legacy DS1 and DS3 services. Claims that customers do not cross-shop DS1/DS3 services against faster and less expensive best efforts services – which also often also include service level agreements – is simply not credible on its face.

Such claims are also refuted by the record evidence, which confirms that customers frequently do choose the faster and lower priced cable best efforts services over legacy DS1 and DS3 services, and that both ILECs and CLECs have lost a significant number of lower-bandwidth customers to cable best efforts services. USTelecom, for example, has submitted a study showing that very large percentages of small and medium sized businesses consider cable best efforts services to be a substitute for legacy TDM-based services, and that many have indeed switched

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from legacy TDM-based services to best efforts cable services.[38] These survey results are consistent with ILEC experience. AT&T has demonstrated that, for the thirteen month period from November 2014 through November 2015, a very substantial portion of AT&T's competitive losses were to cable companies and a significant portion of those losses were to best efforts cable services.[39] CenturyLink has reported that it "competes against all major cable companies, including but not limited to Comcast, Cox, Time Warner Cable, Charter, and Brighthouse," including against these cable companies' "best efforts services" offerings.[40] CLECs have reported similar competitive pressure for cable companies' best efforts services. XO's Director of Product Analytics has emphasized that XO is "regularly competing" against cable companies for small and medium sized businesses, that it "loses" small and medium-sized customers "to [cable] companies offering Best Efforts Internet," and that it has developed "products to this group of customers."[41] Similarly, Windstream's website advertises its "Ethernet Internet" service (with a 99.99% uptime guarantee) as a substitute for best efforts cable.[42] TDS has likewise indicated that the vast majority of customers purchase lower-bandwidth services from TDS and that these customers have been "downgrading to best efforts broadband internet access services for cost savings."[43]

AT&T and other ILECs have also demonstrated that they are now significant *purchasers* of cable company best efforts services as inputs to the data services they sell to retail customers. AT&T for example, has explained that it currently has contracts with **[BEGIN HIGHLY CONFIDENTIAL]** [redacted] **[END HIGHLY CONFIDENTIAL]** for the purchase of HFC-based "services outside of AT&T's ILEC footprint," and that it has certified these services for use as inputs to AT&T's flagship MIS, VPN and backhaul services.[44] Similarly, CenturyLink has demonstrated that "as a buyer of access, CenturyLink has

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[38] *See* Letter from Diane Griffin Holland (USTelecom) to Marlene H. Dortch (FCC), WC Docket Nos. 16-143, 05-25, RM-10593 (Aug. 9, 2016) (attaching survey results).

[39] Reply Comments of AT&T Inc., *Special Access Rates for Price Cap Local Exchange Carriers*, *et al.*, WC Docket No. 05-25, RM-10593, at 26-27 (filed Feb. 19, 2016) ("AT&T 2/19/16 Reply").

[40] Reply Comments of CenturyLink, *Special Access for Price Cap Local Exchange Carriers*, *et al.*, WC Docket No. 05-25, RM-10593, at 9-10 (filed Feb. 19, 2016) ("CenturyLink 2/19/16 Reply").

[41] Declaration of James A. Anderson, ¶ 33, attached to XO 1/27/16 Comments.

[42] *See* Windstream, Ethernet Internet, available at http://www.windstreambusieness.com/products/enterprise-network-servides/dedicated-internet-services/ethernet-internet.

[43] Declaration of James Butman on Behalf of TDS Telecommunications Corp., ¶¶ 5, 15 (Butman 3/26/15 Decl."), attached to Letter from Thomas Jones (TDS) to Marlene H. Dortch (FCC), *Special Access for Price Cap Local Exchange Carriers*, *et al.*, WC Docket No. 05-25, RM-10593 (filed Mar. 26, 2015) ("TDS 3/26/15 *Ex Parte*").

[44] AT&T 3/21/16 *Ex Parte* at 7-8.

entered into various arrangements with cable companies, and has, over time, increased the volume of HFC-based services it acquires from them because of the value proposition they offer."[45]

When all BDS competitors are considered, the record shows that the pricing flexibility triggers were highly under-inclusive, in the sense of leaving areas with sunk facilities and multiple competitors under unnecessary price cap regulation.[46] As a result, there is a clear and pressing need to extend Phase II pricing flexibility to additional MSAs. There are many MSAs still subject to price cap regulation where, according to the 2013 data, ILECs face competition for the vast majority of customers. To take one of the starkest and most indefensible examples in AT&T's territory, the Chicago MSA is still subject to price caps even though the 2013 data show that more than *96% of all buildings* served by an ILEC in the Chicago MSA are within 2,000 feet of at least one competitive provider (*e.g.*, CLEC or cable fiber facilities or cable HFC facilities). And these data understate the true extent of competition *today*, because these 2013 data do not account for the explosive growth and facilities investment undertaken by cable companies and other Ethernet providers over the last four years.[47] Having now collected the data, the Commission would have no lawful justification for continued price cap regulation in the most intensely competitive MSAs in the nation.[48]

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[45] CenturyLink 2/19/16 Reply at 11-12.

[46] Accounting for all relevant competitive facilities, which include the cable company connection data from the National Broadband Plan mapping project, competitors as of 2013 had deployed their own competitive facilities in nearly all census blocks (95.2 percent) *nationwide* that contain special access demand, and those census blocks, in turn, account for virtually every special access connection (97 percent) and business establishment (98.9 percent). IRW 1/27/16 White Paper, Section III.B.

[47] *See, e.g.*, AT&T 1/27/16 Comments at 11-17. The rate of growth by competitive providers is evident even *within* the data collection. According to the data, between January and December of 2013, competitive provider circuit element counts increased by 12.3 percent and number of customers increased by 8.8 percent. During that same time period, these measures shrank for incumbent LECs by 3.3 percent and 6.2 percent, respectively. Additionally, total in-cycle monthly billings increased by 10.3 percent for competitive providers, compared to an increase of 6.3 percent for incumbents. The growth in Ethernet bandwidth mirrors this pattern. From January to December 2013, competitive Ethernet bandwidth increased by 31.6 percent, while incumbent bandwidth grew by just 5.3 percent. And these figures are almost certainly a gross under-estimation of competitive provider bandwidth growth, because the data collection masks bandwidth measures above 1 Gbps. IRW Jan. 26 White Paper at 22-23.

[48] *See, e.g.*, *Motor Vehicle Mfrs. Ass'n of United States, Inc.* v. *State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983) (to engage in reasoned decisionmaking, an agency "must examine relevant data"); *Butte County, Cal.* v. *Hogen*, 613 F.3d 190, 194 (D.C. Cir. 2010) ("an agency's refusal to consider evidence bearing on the issue before it constitutes arbitrary agency action within the meaning of § 706"); *Comcast Corp.* v. *FCC*, 579 F.3d 1, 7 (D.C. Cir. 2009) (vacating Commission rule that capped the market share of any single cable television operator at 30% of subscribers because the Commission "fail[ed] to consider the impact of [direct broadcast satellite] companies' growing market share" and "the growth of fiber optic companies"); *Illinois Pub. Telecomm. Ass'n* v. *FCC*, 117 F.3d 555, 564

*Relief on an MSA Basis*. The Commission should also retain the MSA as the geographic basis for relief, for several reasons. First, insisting on more geographically granular regulation would impose unreasonable burdens on the industry.[49] AT&T maintains dozens of IT applications to manage sales, ordering, billing, and tracking of BDS services, both within and outside of its region. These systems are highly interdependent and frequently work in tandem, which means that the fields and identifiers in these systems must be consistent across the entire system architecture. Today, all BDS locations for AT&T's legacy TDM services are tracked in AT&T's ordering and billing applications by their Common Language Location Information ("CLLI") codes (*i.e.*, wire center identifiers), which in turn link to look-up tables that cross-reference the record's CLLI code with the appropriate MSA and regulatory status.

If the Commission shifted to a regime that provided relief on a geographic unit smaller than an MSA, such as a county, AT&T would have to overhaul numerous legacy RBOC and AT&T systems to comply with such a regime. AT&T would have to build from scratch a new data repository, similar to the current CLLI/MSA repository, which AT&T's sales, ordering and billing applications could use to match the service to the geographic region and thus to the correct regulatory status. AT&T would then have to modify dozens of inter-dependent sales, billing, and ordering applications (comprising thousands of program components) to enable them to utilize the new data repositories. The costs and challenges of such a fundamental overhaul would be compounded by numerous factors, including the facts that (1) many of these systems are decades old and are written in older programming languages; (2) each of AT&T's legacy regional operating companies has its own unique version of these systems that would have to be updated independently; and (3) many AT&T customers maintain their own BDS ordering applications, which would have to be analyzed and possibly updated as well in order to interface properly with AT&T's modified systems. AT&T estimates that full implementation and testing of such changes to these interdependent systems would require many months to complete and would cost millions of dollars.[50] Moreover, as implementing these expensive changes to AT&T's systems would be time-consuming,[51] consumers would not reap the substantial benefits of the Commission revised pro-competitive BDS regulations for some time. And, at the end of the day, there is simply no

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(D.C. Cir. 1997) (vacating Commission rates for certain types of payphone calls because the Commission "failed to respond to any of the data showing that the costs of different types of payphone calls are not similar").

[49] These systems and the necessary changes are explained in greater detail in the Declaration of Martin Kelly ("Kelly 10/6/16 Decl."), attached to Letter from Chris Shenk (representing AT&T) to Marlene H. Dortch (FCC), *Business Data Services in an Internet Protocol Environment, et al.,* WC Docket Nos. 16-143, 05-25, RM-10593 (Oct. 6, 2016) ("AT&T 10/6/16 *Ex Parte*").

[50] Kelly 10/6/16 Decl. ¶¶ 12-13.

[51] *Id.*

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good reason to *require* any ILEC to undertake such costly and extensive changes merely to modify the regulatory treatment of TDM-based services, given that those services are experiencing rapid declines and are scheduled to be retired altogether early in the next decade.

Nor is there any *regulatory* reason to abandon MSAs. The CLECs' objection to MSAs has been that the original triggers were based on proxies that could overstate the actual amount of competition. The Commission predicted that the existence of widespread collocations was a good proxy for building-level competition in the MSA, and the D.C. Circuit upheld this approach as a reasonable predictive judgment about where competition would permit deregulation.[52] The CLECs, however, have argued that the existence of collocations in 65 percent of wire centers is no guarantee of wide-spread *building*-level competition in the MSA. As discussed above, although AT&T disputes that the original triggers were overinclusive (and in fact, if anything the record shows they were underinclusive), AT&T's proposed approach addresses this concern, because it does not rely on predictions or proxies. Rather, AT&T's test would grant Phase II relief only in MSAs where, according to granular, building-level data, at least 80 percent of the specific *locations* are addressable by existing competitive facilities. There is no prediction here – the data collected ensures that this approach results in regulatory relief only in areas where the overwhelming majority of buildings (and an even larger percentage of demand) are subject to competition.

Any geography the Commission could pick will necessarily involve trade-offs between the administrative costs of different proposed approaches and the possible benefits. In this instance, the costs of a wholesale change in an ILEC's billing and ordering systems – particularly for services that are in their last throes of existence – would far outweigh any conceivable improvements in the "accuracy" of the Commission's price cap regime applicable to DS1 and DS3 channel terminations. Accordingly, the Commission should retain the MSA as the geographic basis for relief. As explained above, the extremely high location percentage AT&T has proposed for its MSA test will ensure that relief is not "over-inclusive."

*Number of Competitors*. Some proponents of regulation have argued that a test based on one competitor would be insufficient to ensure competitive outcomes, but those arguments run counter to basic economics and years of Commission, court, and DOJ precedent. Indeed, just four months ago, the Wireline Bureau rejected any such notion in the Verizon/XO merger proceeding, when it found competition in buildings where there is at least one other competitor *near* a

[52] *WorldCom*, 238 F.3d at 458-59.

building.[53] Likewise, the D.C. Circuit has explained that "the presence of facilities-based competition with significant sunk investment makes exclusionary pricing behavior costly and highly unlikely to succeed," because "that equipment remains available and capable of providing service in competition with the incumbent, even if the incumbent succeeds in driving that competitor from the market."[54] These findings are consistent with the Department of Justice's approach in merger cases, where it has also concluded that the presence of a single competitor is sufficient to make the threat of anticompetitive harm unlikely. For example, in prior AT&T and Verizon Consent Decrees, the Justice Department found that the potential for competitive harm existed only in buildings where only "AT&T and SBC or MCI and Verizon, respectively, were capable of supplying local private lines before the merger and *no other competitive LEC* was likely to connect the building to its network."[55] And, as Professors Israel, Rubinfeld, and Woroch have explained, "[a]s a matter of economics, price cap regulation is unnecessary and is, in fact, counterproductive in areas where rivals have deployed competing facilities-based networks."[56]

*Phase I Relief.* Finally, the Commission should immediately grant Phase I pricing flexibility in all remaining areas. Phase I pricing flexibility allows ILECs *downward* pricing flexibility – *e.g.*, the ability to enter into contract tariffs that contain customer-specific term, volume, and other discounts. The legacy price cap regulations' prohibition on lowering ILEC prices was based on a concern about predatory pricing that has no continuing validity today, if it ever did. Such prohibitions serve no purpose today other than to deny customers the ability to negotiate lower prices from the ILEC. This prohibition only harms competition and consumers and should be eliminated everywhere.

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[53] *See Verizon/XO Merger Order* ¶ 22; *see also Pricing Flexibility Order* ¶ 80 (once a facilities-based competitor has "entered the market and cannot be driven out, rules to prevent exclusionary pricing behavior are no longer necessary").

[54] *WorldCom*, 238 F.3d at 458-59 (citing *Pricing Flexibility Order* ¶ 80).

[55] Memorandum Opinion and Order, *AT&T Inc. and BellSouth Corp., Application for Transfer of Control*, 22 FCC Rcd. 5662, ¶¶ 41-42 (2007) (emphasis added; citation omitted).

[56] IRW 1/27/16 White Paper at 13. As a matter of economics, the first competitor would have the largest competitive impact, with additional competitors having only a diminishing effect. Declaration of Mark Israel, Daniel Rubinfeld, and Glenn Woroch, at 13-14 ("IRW 2/19/16 Declaration"), attached to AT&T 2/19/16 Reply. *See also* Rysman White Paper at 218-219; Baker 1/27/16 Decl. ¶¶ 39-40, 43.

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## III. THE RECORD SHOWS THERE IS NO NEED TO RESET THE X-FACTOR, BUT IF THE COMMISSION DOES SO, IT SHOULD SET THE X-FACTOR AT 2.0 PERCENT.

No party has made a case that the Commission needs to establish a new, BDS-specific X-Factor for DSn services. Demand for DSn services are in rapid decline, and carriers are moving toward retiring their legacy TDM facilities. Accordingly, there is no reasonable expectation that LECs will achieve meaningful productivity gains in providing these services in the future. The Commission's policy goal in this proceeding is to encourage the deployment of broadband networks, but arbitrarily increasing the X-Factor to drive down DSn rates would artificially prolong demand for these outmoded services and create incentives for LECs to divert resources toward trying to achieve productivity gains for DSn services – all of which would be directly contrary to that goal.

If the Commission retains Phase I regulation for some DSn services and decides to adopt a new X-Factor, the record overwhelmingly shows that the U.S. Bureau of Labor Statistics' ("BLS") Capital, Labor, Energy, Materials, and Services data ("KLEMS") methodology is the only defensible way to measure BDS productivity of those proposed in the *Notice*.[57] All other suggested methodologies to calculate an X-Factor in the record have been debunked as being mathematically incorrect or based on false presumptions. Under the BLS KLEMS methodology, observed productivity since 2005 has averaged about 2.0 percent, almost perfectly offsetting inflation, which has also averaged about 2.0 percent. Since the current X-Factor has been set equal to inflation

[57] Mark E. Meitzen & Philip E. Schoech, "Assessment of the FCC's Proposed Options for the Special Access Price Cap X-Factor," *Business Data Services in an Internet Protocol Environment, et al.*, WC Docket Nos. 16-143, 05-25, RM-10593, at 5 (filed June 28, 2016) ("Christensen 6/28/16 Paper") ("The KLEMS database is developed using rigorous total factor productivity principles and is a valid source of measuring total factor productivity and input price trends for various industries."); *see also* Appendix 2 to AT&T 8/9/16 Reply (errata filed Aug. 19); Letter from Keith M. Krom (AT&T) to Marlene H. Dortch (FCC), *Business Data Services in an Internet Protocol Environment, et.al.,* WC Docket Nos. 16-143, 15-247, 05-25, RM-10593 (Aug. 16, 2016) (discussing shortcomings of Sprint's EU KLEMS proposal); Letter from Christopher T. Shenk (representing AT&T) to Marlene H. Dortch (FCC), *Business Data Services in an Internet Protocol Environment, et al.,* WC Docket Nos. 16-143, 15-247, 05-25, RM-10593 (Sept. 22, 2016) ("AT&T 9/22/16 *Ex Parte*") (discussing shortcomings of Sprint's second proposed methodology combining BLS KLEMS and CACM inputs); Supplemental Declaration of Mark E. Meitzen and Philip E. Schoech, attached to AT&T 9/22/16 *Ex Parte* (same); Letter from Keith M. Krom (AT&T) to Marlene H. Dortch (FCC), *Business Data Services in an Internet Protocol Environment, et al.,* WC Docket Nos. 16-143, 15-247, 05-25, RM-10593 (Oct. 6, 2016) (debunking Sprint's second X-factor calculation proposal); Letter from Keith M. Krom (AT&T) to Marlene H. Dortch (FCC), *Business Data Services in an Internet Protocol Environment, et al.*, WC Docket Nos. 16-143, 05-25, RM-10593 (Oct. 20, 2016) ("AT&T 10/20/16 *Ex Parte*") and attached Second Supplemental Declaration of Mark E. Meitzen and Philip E. Schoech, Christensen Associates (Oct. 18, 2016) ("Christensen 10/20/16 Declaration") (responding to Sprint's additional proposed X-factor calculation methodology).

over that time period, the actual X-Factor has produced results that are extremely close to the BLS KLEMS measurements.[58]

The Commission then has two options. If the Commission adopts a new X-Factor, it should use the BLS KLEMS methodology to calculate the X-Factor going forward, which the record shows should be no more than 2.0 percent.[59] But it is not clear that there is a compelling need to change the X-Factor at all. Changing the X-Factor to 2.0 percent based on the BLS KLEMS methodology may not be sufficiently different from inflation to necessitate a formal rule change. This is especially true considering that this X-Factor would apply only to a relatively small set of services – under our proposal, only DSn channel termination services in Phase I areas – and those services will be obsolete and replaced within the foreseeable future.

## IV. THE RECORD SHOWS THAT THE ETHERNET MARKET IS HIGHLY COMPETITIVE TODAY.

Finally, there is no basis for imposing any new regulations on Ethernet services. First, the Commission would face a high legal bar in adopting any new regulation of Ethernet. The Commission granted forbearance from *ex ante* rate regulation for Ethernet services almost a decade ago, and the D.C. Circuit affirmed those rulings.[60] The Commission granted this relief because it found that "there are a myriad of providers prepared to make competitive offers to enterprise customers demanding packet-switched data services located both within and outside any given incumbent LEC's service territory," including "many competitive LECs, cable companies, systems integrators, equipment vendors, and value-added resellers."[61]

Established Supreme Court precedent requires that when an agency adopts "new policy" which "rests upon factual findings that contradict those which underlay its prior policy," it must

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[58] For this reason, there is no reason to impose a one-time downward adjustment to the caps to capture productivity gains that purportedly were not captured as a result of the X-Factor being "too low" in the years since the CALLS Plan, as some have proposed. *See, e.g.*, AT&T 8/9/16 Reply at 77-81; AT&T 10/20/16 *Ex Parte* at 1-2; Christensen 10/20/16 Declaration at 2-9.

[59] Christensen 6/28/16 Paper at 7-9 & Table 1; Christensen Associates, Reply Comments of Mark E. Meitzen & Philip E. Schoech, *Business Data Services in an Internet Protocol Environment, et al.*, WC Docket Nos. 16-143, 15-247, 05-25, RM-10593, at 1-2 (filed Aug. 9, 2016) ("Christensen 8/9/16 Reply Comments"); Comments of AT&T Inc., *Business Data Services in an Internet Protocol Environment, et al.*, WC Docket Nos. 16-143, 05-25, RM-10593, at 57-58 (June 28, 2016) ("AT&T 6/28/16 Comments").

[60] *AT&T Title II and Computer Inquiry Forbearances*, 22 FCC Rcd. 18705 (2007) ("*AT&T Forbearance Order*"), *aff'd*, *Ad Hoc Telecomms. Users Comm. v. FCC*, 572 F.3d 903 (D.C. Cir. 2009).

[61] *AT&T Forbearance Order* at 18718-18719, ¶ 22.

"provide a more detailed justification than what would suffice for a new policy created on a blank slate."[62] Accordingly, the Commission would have to provide an especially "detailed justification" showing that regulatory intervention is affirmatively necessary in light of changed circumstances – *i.e.*, that the Commission's finding in 2007 that the Ethernet market is highly competitive is no longer valid.

No such showing would be possible here. The record confirms that Ethernet services are not only robustly competitive, but far more competitive than they were in 2007. A wide variety of ILECs, CLECs, cable companies, and others have invested billions of dollars to deploy Ethernet services, and none today has a port share in excess of twenty percent.[63] As of year-end 2016, there were nine Ethernet providers with port shares of four percent or more, and those nine providers include three CLECs and three of the nation's largest cable companies.[64] And other providers – *i.e.*, those with port shares under four percent – together have, in the aggregate, a port share larger than any single provider.[65] ILEC Ethernet market shares have consistently fallen since 2010, while those of the CLECs and cable MSOs have consistently increased.[66] Indeed, "more than 60 percent of new connections were delivered by CLECs and Cable MSOs during the first half of 2016."[67] According to a report by Ovum, Ltd. "North America remains the most dynamic Ethernet market [compared to its European and Latin American counterparts]" and "the greatest number of large-scale data center operators."[68]

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[62] *FCC* v. *Fox Television Stations, Inc.*, 556 U.S. 502, 515 (2009); *see also id.* at 516 ("a reasoned explanation is needed for disregarding facts and circumstances that underlay or were engendered by the prior policy").

[63] Vertical Systems Group, "2016 U.S. Carrier Ethernet LEADERBOARD" (Feb. 23, 2017), available at https://www.verticalsystems.com/vsglb/2016-u-s-carrier-ethernet-leaderboard/ ("Ethernet Leaderboard").

[64] *Id*. *See also Notice* ¶ 83. The Verizon-XO merger combined two of those nine, but the Commission's Wireline, International, and Wireless Bureaus approved their merger without conditions, in part on the ground that Verizon's acquisition of XO within its incumbent LEC territory would have only a *de minimis* impact on competition. *See Verizon-XO Merger Order* ¶ 17; *see also id*. ¶ 20 ("XO's total fiber assets are largely complementary rather than overlapping with Verizon's fiber facilities, approximately 15 percent of which are in Verizon's incumbent LEC region and the remaining 85 percent outside of it").

[65] *See* Ethernet LEADERBOARD.

[66] *See id.*

[67] Vertical Systems Group: Shakeup in Mid-2016 U.S. Ethernet LEADERBOARD, *Charter surges ahead of Verizon into third position due to its acquisitions of Time Warner Cable and Bright House* (quoting Rick Malone, Principal of Vertical Systems Group) (emphasis added) ("2016 Vertical Systems Analysis") (cited in AT&T 8/22/16 *Ex Parte*).

[68] Ovum, "Ethernet Services Forecast Report: 2015-20," at 16 (Sept. 28, 2015).

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The Commission should therefore conclude that the record here confirms what it found in 2007 (and in 2003 when it determined that unbundling these same services was unnecessary) – that the Ethernet market is highly competitive and light touch regulation is the correct means of ensuring that this market continues to grow and thrive. Thus, only limited Title II regulation is necessary for this technology.[69]

## V. Conclusion

The Commission should revise the price cap and pricing flexibility rules as described above and close the proceeding.

Very truly yours,

/s/ James P. Young
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[69] Indeed, one could question, based on the evidence in the current proceeding, whether *any* Title II regulation is necessary for these highly competitive services, especially given that these rules are applied unevenly and irrationally across providers of the same services today.